

SMALL BUSINESS REORGANIZATION ACT (SBRA)

ELIGIBILITY

- Effective Date: February 19, 2020.
- (180 days after enactment)
- An election by a Small Business Debtor, to be on the petition form. (14 days after order for relief in involuntary cases).
- Absent election, the existing Small Business Case provisions will apply.
- Must be a “Small Business Debtor” as defined in § 101(51D) *as amended*.
- Amendments apply to the definition, whether or not Subchapter V is elected.

SMALL BUSINESS DEBTOR

- A person engaged in *commercial or business activities*.
- Including any *affiliate* of such person that is also a debtor under this *title*.
- Excluding a person whose primary activity is the business of owning ~~or operating real property or activities incidental thereto~~ *single asset real estate*.
- That has aggregate noncontingent liquidated secured and unsecured debts as of the date of the filing of the petition or the date of the order for relief in an amount not more than **\$2,725,625** (excluding debts owed to 1 or more affiliates or insiders)
- ~~For a case in which the United States trustee has not appointed under section 1102(a)(1) a committee of unsecured creditors or where the court has determined that the committee of unsecured creditors is not sufficiently active and representative to provide effective oversight of the debtor.~~
- *and not less than 50 percent of which arose from the commercial or business activities of the debtor.*
- does not include any member of a *group of affiliated debtors* that has aggregate noncontingent liquidated secured and unsecured debts in an amount greater than \$2,725,625 (excluding debt owed to 1 or more affiliates or insiders); Not publicly traded.
- The CARES Act temporarily increased the debt limit to \$7.5 million. This increase is temporary and will sunset on March 27, 2021.

AFFILIATE

DEFINITION

- (2) The term “affiliate” means—
- (A) entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than an entity that holds such securities—
- (i) in a fiduciary or agency capacity without sole discretionary power to vote such securities; or
- (ii) solely to secure a debt, if such entity has not in fact exercised such power to vote.
- (B) corporation 20 percent or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the debtor, or by an entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor, other than an entity that holds such securities—

- (i) in a fiduciary or agency capacity without sole discretionary power to vote such securities; or
- (ii) solely to secure a debt, if such entity has not in fact exercised such power to vote.
- (C) person whose business is operated under a lease or operating agreement by a debtor, or person substantially all of whose property is operated under an operating agreement with the debtor; or
- (D) entity that operates the business or substantially all of the property of the debtor under a lease or operating agreement. A person engaged in *commercial or business activities*.

AFFILIATE PROVISION

- Individual is a “Small Business Debtor” if s/he owns $\geq 20\%$ of a non-SARE corporate debtor
- EVEN IF the corporate debtor files under Chapter 7
- EVEN IF the individual does not meet the 50% threshold.
- PROVIDED the *TOTAL* debt of the individual and the corporation are below the debt limit.

PROS AND CONS OF ELECTING SBRA STATUS

ELECT

- Potential to modify principal residence debt under certain circumstances.
- Voting not required.
- No UST fees (particularly relevant to sale or refinance of valuable real property).
- No creditor plans.
- No absolute priority rule.

NOT TO ELECT

- Trustee *and* UST looking over your shoulder.
- Payment of Trustee and Trustee’s counsel.
- Disposable income requirement (even for corporations, even absent unsecured creditor objection).
- 300 days to file plan instead of 90.
- Discharge upon confirmation, for corporate debtors.

TRUSTEE

- Act allows for standing trustee or appointment by UST of a “disinterested person.”
- UST nationally has elected to select “pools” (not “panels”) from which trustees will be appointed.
- No requirement that the Trustee needs to be a lawyer. UST considering persons with business expertise to “assist” the Debtor.
- Debtor is a Debtor in Possession with full powers.
- No creditor committee unless the Court *for cause* appoints one. Unlike prior law, appointment of a committee does not change Small Business Debtor status.

TRUSTEE RESPONSIBILITIES

- Be accountable for all property received.
- examine and object to proofs of claim “if a purpose would be served”;

- if advisable, oppose the discharge of the Debtor (except that the provisions for denial of discharge were largely written out of the SBRA);
- furnish info to parties in interest; and make a final report.
- perform the duties specified in paragraphs (3), (4), and (7) of section 1106(a) of this title, ***if the court, for cause*** and on request of a party in interest, the trustee, or the United States trustee, ***so orders***.
- These are some of the duties of a Ch11 trustee appointed for cause.
 - Investigate the debtor.
 - file a statement of such investigation.
 - file post-confirmation reports.
- Appear and be heard at the status conference under section 1188 of this title and any hearing that concerns—
 - (A) the value of property subject to a lien.
 - (B) confirmation of a plan filed under this subchapter.
 - (C) modification of the plan after confirmation; or
 - (D) the sale of property of the estate.
- Ensure that the debtor commences making timely payments required by a plan confirmed under this subchapter.
- Committee Report states that “The trustee must perform many of the same duties performed by a chapter 12 trustee. In a chapter 12 case, for example, the trustee serves as a fiduciary for creditors and is accountable for all property of the debtor as well as for ensuring the debtor makes the payments as required by debtor’s reorganization plan.”
- If the debtor ceases to be a debtor in possession, perform the duties specified in section 704(a)(8) and paragraphs (1), (2), and (6) of section 1106(a) of this title, including operating the business of the debtor.
 - Operate the business, file tax returns, provide DSO notices, perform ERISA plan obligations, health care business duties; file schedules; and furnish tax return information.
 - ***These would only apply if the Debtor is removed as DIP for cause.***
- If there is a claim for a domestic support obligation with respect to the debtor, perform the duties specified in section 704(c) of this title; and
- Facilitate the development of a consensual plan of reorganization.
 - Note that the trustee’s services (and compensation) are terminated upon substantial consummation (i.e., typically, commencement of payments) if a plan is confirmed consensually, without cramdown, so this would mean the trustee is working against self-interest.

PAYMENT AND COMPENSATION OF TRUSTEE

Payment

- No requirement for a Debtor to pay the trustee anything before confirmation.
- If anything paid pre-confirmation, trustee shall pay per the plan. If not confirmed, the Trustee may retain funds to pay administrative expenses including trustee compensation.
- If the plan is confirmed through cramdown rather than consent of all classes, ***except as otherwise provided in the plan or in the order confirming the plan***, the trustee shall make payments to creditors under the plan.
- Consensual plans do not require trustee involvement in payments.

Compensation

- If standing trustee, to be paid as Chapter 12/13 standing trustees are paid.

- Provision for compensation of standing trustee “consistent with services performed by the trustee and the limits on the compensation of the trustee established pursuant to paragraph (1) of this subsection” if services terminated by dismissal, conversion, or substantial consummation of consensual plan.
- No special provision for compensation for non-standing trustee. Limitations in § 326 do not apply. Compensation is per § 330.
- Trustee may retain counsel.

PLANS AND CONFIRMATION

- Disclosure statements are NOT REQUIRED unless the Court so orders.
- Replaced by requirement that the plan include:
 - (A) a brief history of the business operations of the debtor;
 - (B) a liquidation analysis;
 - (C) projections with respect to the ability of the debtor to make payments under the proposed plan of reorganization.
- Court can “for cause order otherwise.”
 - If the Debtor is going to try to propose a consensual plan and confirm by voting without cramdown (to get an immediate discharge, to avoid disposable income requirements, to avoid the trustee going forward, etc.), it seems likely that the Court will require disclosure before voting.
- If a disclosure statement is required, Court may allow a combined plan/DS, use of the standard small business forms, and conditional approval.
- Only the Debtor may file a plan.
- Only the Debtor may modify a plan.
 - Only the Debtor can modify, but if confirmation was consensual and any accepting class changes its vote, a modified plan cannot be confirmed.

PLAN DEADLINE

- 90 days after the order for relief under this chapter
- Court may extend the period if the need for the extension is attributable to circumstances for which the debtor should not justly be held accountable.
- No further deadlines for consideration or confirmation of the Plan, as in non-Subchapter V small business cases.

CONFIRMATION

- Consensual confirmation:
 - Requires a vote and acceptance by all impaired classes.
 - All requirements of § 1129(a) other than (a)(15) (disposable income) must be met.

CRAMDOWNS

- Cramdown allowed where the following 1129(a) requirements are not satisfied:
 - (a)(8) (all classes accept)
 - (a)(10) (at least one accepting impaired class);
 - (a)(15) (disposable income if unsecured creditor objects)
- NO ACCEPTING IMPAIRED CLASS IS REQUIRED
- NO VOTE IS REQUIRED
- Notice and opportunity to object still required.

REQUIREMENTS

- Must not discriminate unfairly,
- Must be fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.
- Secured claims:
- § 1129(b)(2)(A), fair and equitable as to secured claims, remains unchanged.
- General requirements for “fair and equitable”:
 - No absolute priority rule for “fair and equitable”.
 - 3-5 years of projected disposable income must be applied to make payments under the plan, OR the value of property to be distributed must not be less than projected disposable income.
 - feasibility requirement with provision for remedies if feasibility is uncertain.
 - No express requirement that these “payments under the plan” from disposable income go to unsecured creditors.
 - No alternative for paying claims in full.
 - No prohibition on retaining or paying equity interests (or paying subordinated debt) if general unsecured creditors are not paid in full.
 - Requirement to prefer preferred stock is eliminated.
- But see 1141(d)(1)(B) – equity interests terminated (this was not written out for 1191(a) consensual confirmations, so needs to be addressed to retain equity interests).

DISPOSABLE INCOME

- Disposable income is NOT defined by Chapter 13 standards.
- Disposable income means the income that is received by the debtor and that is not reasonably necessary to be expended for
 - the maintenance or support of the debtor or a dependent of the debtor; or
 - a post-petition DSO
 - payment of expenditures necessary for the continuation, preservation, or operation of the business of the debtor.
- NO EXCLUSIONS FOR:
 - Social security or VA disability (CMI is not starting point)
 - Child support received.
 - Charitable contributions.
- No “means test” lookback or fake expenses.

DISCHARGE

- If confirmation is consensual under § 1191(a), discharge is upon confirmation, even for individuals.
- If crammed down, discharge is after 3-5 years of payments.
- No felony exception to discharge.
- 727 discharge denial grounds will not deny a discharge even in a liquidating case,
- Debtor Ed certificate not required, but only if crammed down, or not liquidating.
- DOES NOT discharge debt that is to be paid longer than the 3-5 year term.
- DOES NOT discharge § 523(a) debt *ARGUABLY EVEN IN CORPORATE CASES*.

ADMINISTRATIVE REQUIREMENTS AND EXPENSES

REQUIREMENTS

- Same small business case opening documents must be filed.
- Same Monthly Operating Report requirement.
- Same requirement to attend IDI, maintain insurance, file, and pay taxes and DSOs.
- Status conference is mandatory.

ADMINISTRATIVE EXPENSES

- Notwithstanding section 1129(a)(9)(A) administrative expenses and involuntary gap claims may be paid “through the plan,” but only if confirmed under the cramdown provisions.
 - if confirmed under (a), must be paid on the effective date absent agreement.
- What “through the plan” means is not clear, but presumably it allows the lawyer and other admin and gap creditors to get paid over time from payments to the trustee.

REMOVAL AS DIP

- Debtor may be removed as debtor in possession for cause, ***including*** fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor, either before or after the date of commencement of the case, or for failure to perform the obligations of the debtor under a plan confirmed under this subchapter.
- On request of a party in interest, and after notice and a hearing, the court may reinstate the debtor in possession.
- Conversion and dismissal provisions of Chapter 11 also apply.

PRINCIPAL RESIDENCE MODIFICATION PROVISIONS

- Notwithstanding section 1123(b)(5) of this title, Plan may modify the rights of the holder of a claim secured only by a security interest in real property that is the principal residence of the debtor if the new value received in connection with the granting of the security interest was—
 - (A) not used primarily to acquire the real property; and
 - (B) used primarily in connection with the small business of the debtor.
- Includes HELOCs and other second mortgages, and cash-out, and does not require that the lender have a business purpose in mind.